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24 September 1974

MEMORANDUM FOR: [redacted]

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SUBJECT : Contribution to Interagency Memorandum on Portugal

Attached are the sections you requested on the current economic situation in Portugal and the economic impact of freeing the African colonies. If you need any further information, please [redacted]

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Office of Economic Research

Attachment: As Stated

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PORTUGAL: THE ECONOMIC IMPACT OF LOSING ANGOLA, MOZAMBIQUE, AND PORTUGUESE GUINEA

SUMMARY

Angola, Mozambique, and Portuguese Guinea as a group clearly have been net economic liabilities to Portugal in recent years. The costs to Portugal were mainly attributable to the guerrilla wars. The cost of military operations in Africa has been equivalent to perhaps 3% of Portugal's GNP and these operations have diverted about 4% of its labor force into the armed forces. In other respects, economic relationships between the Metropole and the three territories have been fairly well balanced and, probably, mutually beneficial. If the move toward independence follows its present course, these relationships -- both private and governmental -- will not be severely disrupted.

At home, Portugal faces severe economic problems stemming from the new government's failure to provide economic leadership. The self-made problems are compounded by the adverse balance-of-payments effects of a higher oil import bill and of the loss of foreign exchange earnings from tourism and from expatriate Portuguese workers as economies slump elsewhere. The slack in Portugal's economy will reduce one of the immediate benefits expected from the cut in military operations, because discharged soldiers will have great difficulty finding civilian jobs.

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TRADE WITH THE TERRITORIES

Trade between Portugal and the three territories appears to be mutually beneficial, with neither side having a particular advantage. In recent years, Portugal has run annual trade deficits with the group ranging as high as $75 million. The deficits have resulted mainly from trade with Angola. Trade with Mozambique has been roughly in balance and there is regularly a surplus with Portuguese Guinea. But with the Portuguese economy's rapid expansion and the development of its trade with other West European countries, the colonies' relative importance in Portugal's trade has declined rapidly. The three areas' share of Portugal's exports dropped from 23% in 1970 to 10% in the first four months of this year; their share of Portugal's imports fell from 14% to 9%. The Metropole remained the key trading partner of the three territories in 1973, taking about 25% of Angola's exports, 30% of Mozambique's, and 90% of Portuguese Guinea's.

Both sides enjoy some special privileges in the trading relationship. Portuguese exports, though subject to tariffs, find a sheltered market in the territories. Goods from the three areas -- of which coffee, sugar, bananas, and crude oil are the most important -- normally enter Portugal duty-free. The most valuable special privilege to

MILITARY COSTS

The main burden on Portugal of keeping the three African colonies has been the cost of fighting guerrilla movements. The overall military budget in 1974 is about $580 million -- 27% of the total budget and equivalent to about 6% of GNP. Nearly 40% of the military budget (some $220 million) is for overseas military operations. Allowing for Lisbon's habitual underestimation of government spending in its budget proposals, the true financial cost of the wars is probably close to $300 million annually. In terms of manpower, Portugal keeps about 250,000 men in uniform -- about 8% of the total labor force. Half of these troops are stationed in Africa. In normal circumstances, the men now in Africa could be holding productive civilian jobs, either in Portugal or elsewhere in Western Europe. At present, however, economic conditions in Portugal are chaotic and unemployment is rising elsewhere in Europe. With jobs scarce, the immediate benefit from releasing men from military service would be reduced. There would still be some economic gain even if all the returned soldiers are kept in uniform because they will be spending more of their wages in Portugal, providing some stimulus to the domestic economy and reducing the flow of funds out of the country.

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Portugal is its option of purchasing up to one-half of Angola's crude oil production. It was this provision that effectively shielded Portugal from the Arab oil embargo last winter. Portugal reportedly pays relatively low prices for coffee and tobacco from the territories but the total value of this benefit appears to be small -- perhaps $10 million annually for Angolan products and much less for those from Mozambique. The Metropole is currently getting sugar from Mozambique at a bargain -- about one-fourth the world price, equivalent to an $80 million annual saving. Arising from contracts signed prior to the recent spectacular rise in world sugar prices, this windfall will not endure. Indeed, until recently, Portugal was paying a premium price for Mozambique's sugar.

FINANCIAL FLOWS

The net flow of payments for services and unilateral transfers between Portugal and its Overseas Provinces[1] was nearly in balance in 1973. Portugal receives a substantial net inflow of foreign exchange from such items as foreign travel, investment income, and private transfers. These receipts are offset by large government transfers to the provinces -- $180 million in 1973.

[1] It is not possible to separate the three African territories in question, but they account for an overwhelming share of transactions between Portugal and the Overseas Provinces.

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With respect to long-term movements of capital, there was a substantial net flow of funds from Portugal to the Overseas Provinces. The net outflow in 1973 was $88 million, nearly all official. Short-term capital flows are quite small, perhaps because of the exchange controls within the escudo zone.

THE ESCUDO ZONE AND THE BALANCE OF PAYMENTS

There will be a small net disadvantage for Portugal if the escudo zone -- consisting of Portugal and its overseas territories -- breaks up. Angola has a large trade surplus with third countries, and the foreign exchange reserves it earns and turns over to Portugal strengthen the Portuguese escudo. Even without this help, however, Portugal's own balance-of-payments position has been very strong in recent years. The current account surplus in 1973 was about $600 million, a very large amount for an economy of Portugal's size. Admittedly, higher oil costs will cut the current account surplus by half, and the current economic disruptions in Portugal will further erode it. Nonetheless, over the next few years, Portugal will probably have one of the stronger payments positions in Western Europe, if there is at least a semblance of domestic economic order.

THE WHITE SETTLERS

The one way in which loss of the colonies could impose a severe immediate burden on Portugal would be through a mass return of white settlers. There are approximately 400,000 such people in the three areas, most of them Portuguese. If a majority chose to return to the Metropole, Lisbon would have enormous difficulty trying to feed, clothe, house, and employ them on top of its other economic problems. It appears, however, that most of the settlers will stay in Africa. Most want to stay and their skills certainly will be needed there.